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No. 03-59

IN THE

Supreme Court of the United States

BAXTER INTERNATIONAL, INCORPORATED,
Petitioner,

v.

ABBOTT LABORATORIES,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

PETITIONER'S REPLY BRIEF

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PETITIONER'S REPLY BRIEF

Abbott's Brief in Opposition badly obscures the nature of this case. Abbott would have this Court believe this is an antitrust case. Br. in Opp. 1 (arguing Baxter contended that its defense "arose under federal antitrust law"), 8 ("antitrust affirmative defense"), 9 (same), 11 ("issue of federal antitrust law"), 12 ("a federal antitrust issue"), 14 ("antitrust affirmative defense"). It is not. This Court has made clear that a party raising a public policy defense to enforcement of an arbitral award must point to some "positive law" violated by the award. *Eastern Associated Coal Corp.* v. *United Mine Workers of Am., Dist. 17*, 531 U.S. 57, 63 (2000). Baxter pointed to the two sources of positive law implicated by the arbitrators' ruling: the antitrust laws and the FTC/Abbott Consent Decree. Had the arbitrators interpreted the contract to require Baxter to rob a bank, Baxter would have pointed to state and federal criminal law. From the point of view of the

public policy defense, the particular positive law the award compels a party to violate is a detail.

The central thrust of Abbott's Brief in Opposition is, thus, a distraction. Baxter did not attempt to relitigate in court an "antitrust claim" presented to and ruled upon by the arbitrators. And Baxter never "recast[]" an antitrust claim as a public policy question. See Br. in Opp. 14. Baxter has consistently presented its argument as one seeking to protect public policy, which happens to be embodied in the antitrust laws and in a consent decree.

The true nature of this case is quite simply stated: This is a contract case that was submitted to arbitration. Therefore, the following rules apply. In a contract case, a party is permitted to argue that its opponent's interpretation of the contract should be rejected because it would render the contract unlawful and hence contrary to public policy. *West Bend Mut. Ins.* v. *Mulligan Masonry Co.*, 786 N.E.2d 1078, 1088 (Ill. App. Ct. 2003).[1] Baxter thus urged the arbitrators to reject Abbott's proposed interpretation of the Sevoflurane and Dispute Resolution Agreements because Abbott's reading would render the contracts unlawful and hence contrary to public policy. After the arbitrators ruled, the question before the federal courts was whether to enforce the award. In an arbitration case, a party is permitted to argue against judicial enforcement of an award if it compels the parties to violate the law and hence public policy. *United Paperworkers Int'l Union* v. *Misco, Inc.*, 484 U.S. 29, 43 (1987); *W.R. Grace & Co.* v. *Local Union 759*, 461 U.S. 757, 766 (1983). Baxter thus urged the district court, and the court of appeals, to refuse to enforce the arbitration award because, by adopting Abbott's interpretation of the contract, the arbitrators compelled Baxter (and Abbott) to violate the law and hence public policy.

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[1] Illinois law controlled the interpretation of the contract.

The district court recognized its obligation to review the award to ensure that it did not compel a violation of public policy. The Seventh Circuit, over a dissent from one member of the panel and three members of the full court asked to rehear the case *en banc*, has held that when an arbitrator rejects a public policy contract defense, a court may not consider a public policy defense to enforcement of the arbitral award. As detailed below and in Baxter's Petition, the conflict between the Seventh Circuit's ruling and those of other courts is real and creates confusion in an area of the law—federal court review of arbitral awards—that demands national uniformity. This Court should grant the petition.

1. The Decision Below Cannot Be Squared With The Decisions Of This Court And Other Courts Of Appeals. Abbott's attempt to square the Seventh Circuit's holding with the decisions of this Court and of other federal courts of appeals fails for a simple reason: Abbott never acknowledges the Seventh Circuit's actual holding. Abbott argues this case involves a straightforward application of *Mitsubishi Motors Corp.* v. *Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985) (holding that antitrust claims that are arbitrated receive the same level of court review as any other claim) because it erroneously believes this case involves an "antitrust claim." Br. in Opp. 12 (arguing that "the *Mitsubishi* Court anticipated the circumstances presented here"). Once it becomes clear that the public policy holding of the Seventh Circuit has nothing to do with the fact that this case involves antitrust law (or a consent decree), the whole argument crumbles.

In fact, to the extent the *Mitsubishi* Court anticipated the circumstances here, it concluded that federal court review of the public policy question is always preserved. In *Mitsubishi*, this Court considered the possibility that a foreign arbitral panel might read certain provisions of a contract as a prospective waiver of the right to pursue antitrust remedies. 473 U.S. at 637 n.19. Such a prospective waiver had long been considered an unenforceable violation of public policy.

Id. (citing cases). This Court made clear that if the arbitral panel interpreted the contracts to include such an unlawful prospective waiver, a federal court would not enforce that award. *Id.*

This Court nowhere suggested that a federal court's hands would be tied if, as might be expected, the antitrust claimant first urged the arbitral panel not to read the contract to waive its right to seek antitrust relief precisely because such a reading would violate public policy. Indeed, this Court had already said that whether an arbitrator is first presented with and rules upon a public policy challenge is irrelevant because, "in any event, the question of public policy is ultimately one for resolution by the courts." *Grace*, 461 U.S. at 766. Later this Court made clear that parties concerned that an interpretation of a contract would violate public policy must argue the point to the arbitrator first, precisely because court review of an award for compliance with public policy always remains available. *Vimar Seguros Y Reaseguros, S.A.* v. *M/V Sky Reefer*, 515 U.S. 528, 540-41 (1995). When this Court in *Vimar* said that it would not have ordered the issue to be presented to the arbitrator unless it was certain that a federal court could subsequently review the award for compliance with public policy, *id.*, it left no doubt that public policy remains ultimately for the courts, no matter how the arbitrators treat the issue.

Abbott tries to distinguish this Court's statements in *Mitsubishi* and *Vimar* by arguing that a prospective waiver of statutory remedies is a "distinct circumstance" that justifies federal judicial review of an arbitral award. Br. in Opp. 12-13. But Abbott never explains why. There is no prospective-waiver-of-statutory-remedies defense to enforcement of an arbitral award. Rather, as this Court made clear, the prospective waiver of statutory remedies was important in *Mitsubishi* precisely because such a waiver is a violation of public policy, triggering the public policy defense to enforcement of an award. There is no basis in *Mitsubishi* or

any other case for treating one particular violation of public policy differently than any other violation of public policy. That is, if a court may review an arbitral award to ensure it does not order a prospective waiver of statutory remedies (as Abbott concedes), it also must review an arbitral award to ensure that it does not order a violation of the antitrust laws. The decision below cannot be squared with this Court's decisions outlining the proper role for the courts when presented with public policy challenges to arbitral awards.

Not only is the Seventh Circuit's decision impossible to square with this Court's words, it cannot be squared with the actions of other courts of appeals. Abbott denies that other courts of appeals have reviewed arbitral awards for compliance with public policy even after an arbitrator had been presented with and ruled upon the identical legal issues that make up the public policy defense. Abbott asserts that in the cases cited by Baxter, "the arbitrators were not authorized to, and did not, decide the issues later presented to the courts."[2] Br. in Opp. 13. This assertion is wrong.

In fact, the arbitrators and the courts in the cases cited by Baxter were presented with arguments that mirror Baxter's presentation to the arbitrators and the courts in this case. In all the cases, including this one, the arbitrators were asked to interpret the parties' contract. The labor arbitration cases involved an interpretation of the phrase "just cause," and this case involved an interpretation of the phrase "impairment of the original commercial relationship." In all the cases, including this one, the arbitrators were asked to reject one party's interpretation of the contract in light of certain positive law. The labor arbitration cases involved federal

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[2] Abbott cites no authority for the proposition that an arbitrator lacks the authority to consider whether a proposed interpretation of a contract should be rejected because it would violate public policy. There is none. Arbitrators are free to consider any legal issues presented in support of or against a party's interpretation of a contract.

safety regulations, and this case involved the antitrust laws and the consent decree. *International Bhd. of Elec. Workers, Local 97* v. *Niagara Mohawk Power Corp.*, 143 F.3d 704, 709 (2d Cir. 1998) (stating that the arbitrator "examined at length the Company's [interpretation] within the context of ... NRC regulations"); *Southern Cal. Gas Co.* v. *Utility Workers Union of Am., Local 132*, 265 F.3d 787, 792 (9th Cir. 2001) (stating that the arbitrator "concluded that the Gas Company failed to comply with the strict requirements of the federal regulations regarding DOT drug testing"); *Delta Air Lines, Inc.* v. *Airline Pilots Ass'n*, 686 F. Supp. 1573, 1575 (N.D. Ga. 1987) (stating that arbitrator considered the pilot's compliance with FAA regulations regarding consumption of alcohol by pilots), *aff'd*, 861 F.2d 665 (11th Cir. 1988). And in all the cases, including this one, the federal courts were later asked to review the arbitrators' awards for compliance with the same positive law that had been presented to the arbitrators. The Second, Ninth, and Eleventh Circuits all undertook their own independent reviews of the applicable (and previously presented) positive law to ensure the awards' compliance therewith. *Electrical Workers*, 143 F.3d at 715-19; *Southern Cal. Gas Co.*, 265 F.3d at 795-96; *Delta Air Lines, Inc.* v. *Air Line Pilots Ass'n, Int'l*, 861 F.2d 665, 672-74 (11th Cir. 1988). In stark contrast, the Seventh Circuit refused. There is no way to reconcile the approach of the other courts of appeals with that of the Seventh Circuit.

It is worth noting that none of the other courts considered it significant that the substantive legal issues that form the public policy challenge had been considered by the arbitrators at the employers' invitation. Abbott, on the other hand, appears to attach some significance to the fact that Baxter presented the antitrust and consent decree issues to the arbitrators, at least if repetition is any indication of significance. Br. in Opp. 1 (noting Baxter "submitted" the issues to the arbitrator), 8 ("petitioner expressly invited the tribunal" to consider the issues), 9 (arbitrators considered

issues at "petitioner's own express invitation"), 10 (arbitrators considered issue at "petitioner's own invitation"), 11 (same). This numbing repetition does not, however, reveal what relevance the point has to this case.

Perhaps Abbott believes it best for parties to withhold from the arbitrators a public policy rationale for rejecting a proposed contractual interpretation so that the public policy argument can be presented exclusively to a court. Abbott does not, however, explain why courts should adopt a rule that discourages parties from presenting all their arguments to the arbitrators. Indeed, the Fourth and Seventh Circuits have rejected that approach. Those courts have held that the failure to argue an issue before an arbitrator waives judicial review of the award on the ground not presented. *District 17, United Mine Workers of Am.* v. *Island Creek Coal Co.*, 179 F.3d 133, 140 (4th Cir. 1999); *Baltimore & Ohio Chi. Terminal R.R.* v. *Wisconsin Cent. Ltd.*, 154 F.3d 404, 409-12 (7th Cir. 1998). A full airing of the issues before the arbitrator makes sense, even if the courts ultimately will be required to rule on the issue. Hiding legal issues from arbitrators which bear on the questions before them can only hamper their ability to produce proper rulings. Further, presenting the issue to the arbitrator allows the parties to put the relevant facts on the record, which will facilitate court review. Baxter thus properly presented the arbitrators with the public policy issues that it has also properly presented to the courts.

In the end, the Seventh Circuit's rule produces bizarre results. Assume a party's opponent in an arbitration asks the arbitrators to interpret the contract to compel the parties to violate the law (criminal law, the tax code, antitrust law, or any other positive law). Assume further that the party informs the arbitrators that if they adopt the proposed interpretation, a court will not enforce the award because the award would violate the public policy expressed in that law. And assume finally that the arbitrators expressly reject that view. According to the Seventh Circuit, precisely because the

arbitrators were warned of the possibility that a court would refuse to enforce their award and they adopted the controversial interpretation anyway, the court cannot refuse to enforce the award. This makes no sense and threatens to undermine the critical role this Court has reserved for federal courts to police arbitral awards that violate the public policies reflected in positive law.

2. The Seventh Circuit Has Not Decided The Antitrust Issue. Abbott lastly argues that this Court should decline to review this case because the Seventh Circuit decided that the arbitration ruling did not create an antitrust violation. Br. in Opp. at 8, 14-16. This is demonstrably false. While Judge Easterbrook's opinion offers passing remarks on the question, his opinion is explicit that those remarks did not reflect his (or the Court's) considered views. The panel majority underscored that it considered the merits of the public policy defense only casually by refusing to consider at all whether the award's conflict with the consent decree warranted setting it aside. Pet. App. 7a. The opinion is crystal clear: the substantive public policy claims are "unnecessary to pursue" because "[a]ll that matters today is that the arbitrators have concluded that the antitrust laws" were not violated by their award. *Id.*

Only one appellate judge offered his considered views on the question, and he concluded that the award, in fact, does violate the antitrust laws. Contrary to the passing, single-paragraph musings offered by the panel majority on the antitrust question, Judge Cudahy's dissent carefully analyzes the facts of record against the governing legal standards and concludes that the covenant not to compete imposed by the arbitrators could not have been ancillary to the agreements to produce sevoflurane and could not have had any procompetitive effect. Pet. App. 14a-17a. The antitrust issue presents serious questions that, for the reasons discussed above, a court must confront *de novo* and should not abdicate to arbitrators.

Finally, three of the eight judges of the full Seventh Circuit to review the petition for rehearing *en banc* considered the public policy ruling of the panel sufficiently serious on its own to merit further review. As these judges recognized, the holding of the panel "clouds the authority of [a federal] court to review arbitration agreements of private parties that violate public policy—an authority repeatedly acknowledged by the Supreme Court." Pet. App. 94a. The risk that the decision below will hamper the ability of federal courts to review arbitral awards for compliance with public policy is, by itself, a compelling reason for this Court's review.

CONCLUSION

For the foregoing reasons, and those stated in Baxter's Petition, the petition should be granted.

Respectfully submitted,

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